IN THE

Supreme Court of the United States

OCTOBER TERM, 1949

No. 378

KENNETH J. MULLANE, as Special Guardian and Attorney, etc., *Appellant*

vs.

CENTRAL HANOVER BANK AND TRUST COMPANY, as Trustee, etc., *et al.*

Appeal from the Court of Appeals of the State of New York

BRIEF OF NEW YORK STATE BANKERS ASSOCIATION, *amicus curiae.*

PETER KEBER
Attorney for New York State Bankers Association, amicus curiae.

C. ALEXANDER CAPRON,
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INDEX

Table of Cases

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Statement

This brief is filed by the New York State Bankers Association, as *amicus curiae.*

The New York State Bankers Association is a voluntary association of commercial banks and trust companies (including national banks) in New York State. It numbers approximately six hundred fifty member banks representing more than ninety-five per cent of all the banks in the State.

The New York State Bankers Association is concerned with the outcome of this appeal because of its belief in the importance of the establishment and maintenance of the common trust fund as a vehicle for the investment of small funds. At the present time, in addition to the appellee, ten other banks or trust companies, representing by far the largest volume of trust business in New York State, have

established common trust funds and several others have the matter under consideration. This Association also regards the appeal as important because it appears that the contentions of the special guardian for the income beneficiaries, if sustained, would raise doubts concerning the binding effect of countless numbers of judgments and decrees, which have been rendered by our courts since their inception, judicially settling the accounts of executors, administrators, trustees and other fiduciaries.

It is respectfully submitted that the statement of facts and the arguments made by the respondent, Trustee, are in all respects correct. They are herein adopted.

I.

Certain considerations which prompted the enactment of Section 100-c of the Banking Law of the State of New York permitting and governing the establishment and operation of common trust funds by banks and trust companies.

The following views were the foundation for the legislation which was enacted in New York permitting the establishment of Common Funds by banks and trust companies. (McKinney's Consolidated Laws of New York, Banking Law, Section 100-c). These views have the same force today as they had in 1937 when the statute was enacted.

Small trusts should, if possible, be accorded the same care and judgment in their administration as that which may be enjoyed by larger funds. Persons of small and moderate means should be able to secure the services of corporate trustees which maintain well organized investment departments and trained investment personnel. The need of the beneficiaries of small trusts for a reasonable

return of income is certainly no less than the need of beneficiaries of large trusts. The burden and expense of diversification of investments in a small fund, invested alone, tends to render diversification impractical and to result in investment in low yield premium bonds and frustration of the intention which underlies the grant, now usual in trust instruments, of discretion to invest in nonlegals.

Experience led to the belief that the establishment of Common Funds by corporate fiduciaries would doubtless provide the means of satisfying the needs and requirements of small trusts and of persons of small means. Accordingly, the Board of Governors of the Federal Reserve System modified its rules and regulations with respect to the commingling of trust funds so as to authorize the creation of Common Trust Funds, subject to various limitations and conditions which were deemed adequate to afford protection to the beneficiaries of the estates, trusts and funds which might be invested through the medium of such a Common Fund (Regulation F, Board of Governors of Federal Reserve System, §10(c) and §17). The Federal (Internal Revenue Code, §169) and New York State (McKinney's Consolidated Laws of New York, Tax Law, §365-a) tax laws were amended to permit these funds to be treated as separate entities for certain purposes, but to avoid the features of double taxation which would have arisen had they been treated for all purposes as separate entities, taxable as such.

Thereupon, the New York State Legislature, in 1937, with the guidance and assistance of the Executive Committee of the Surrogate's Association, enacted legislation to authorize the establishment of Common Trust Funds by New York State banks and trust companies. Rigid conditions were attached both by the Legislature and by the regulations, which were subsequently issued by the New York State Banking Board, to avoid prejudice as between various

trusts and funds which might be invested through such a medium, to assure the maintenance of such funds solely for investment purposes, and to assure, so far as that is possible through regulation, the proper administration of such funds (R64-75).

It was then recognized, as it is today, that some system for the economical settlement of the accounts of the trustee of a Common Fund is an essential element of the proper use of such funds. Since the primary purpose of the Common Fund is to fill the needs of small trusts, consideration must be given to such trusts in approaching this matter of accountings.

In New York state, the procedure established with respect to the settlement of the accounts of trustees is exacting in its requirements that the interests of the beneficiaries be fully protected. The notice of the proceeding is designed to give actual, not merely presumptive notice to such beneficiaries. Minors and incompetents must be represented by guardians who are expected to examine the accounts with care and report fully to the court. However, this exacting procedure is not only well calculated to protect beneficiaries, but it is expensive to trusts. It is, therefore, imperative that the expense of these proceedings, particularly with respect to small trusts, should not be increased.

It is respectfully submitted that a small trust whose funds have been invested in a Common Fund cannot possibly afford the expense which would result if, upon the settlement of the account of the trustee of each small trust, it were also necessary to settle the account of the trustee of the Common Fund. The Common Fund may be many millions of dollars. The small trust may have an insignificant amount invested in the Common Fund. If the account of the Common Fund has not been settled, the duty would devolve on the attorneys and guardians of beneficiaries of

the small trust, in an accounting relating to that trust, to examine all transactions in the Common Fund during the period any part of the small trust was invested therein, probably covering a substantial period of years, as well as to determine the condition of the trust at the time the small trust's funds were invested therein (See Matter of Auditore, 249 N.Y. 335, 342). The expense of such examination would be prohibitive.

It was doubtless recognition of this which led the Executive Committee of the Surrogate's Association to recommend a precise and definite system for the settlement of such Common Trust Fund accounts, and not leave that very important subject to be dealt with with by various courts and judges throughout the state in a manner which they might deem adequate. Before recommending Common Trust Fund legislation to the Legislature, the Committee was insistent upon the inclusion of what it deemed practical and adequate safeguards to protect the beneficiaries of all the trusts whose funds might be invested therein, and for notice of the settlement of Common Trust Fund accounts, which would give reasonable assurance that all who wished to participate in the proceedings should have the opportunity to examine the Common Trust Fund accounts and to be heard upon their settlement.

The Committee of the New York State Bankers Association, which from time to time worked with the Executive Committee of the Surrogate's Association, never criticized the statute because the notice was not adequate, but questioned whether all of the requirements with respect to notice were necessary, practical or in the interest of the beneficiaries.

It is the opinion of this Association that very full and adequate provisions have been included in the statute to protect all beneficiaries of all the trusts and funds that may become participants in the Common Fund, and that the system established of giving them notice is reasonably cal-

culated to afford to all persons who desire to appear in the proceedings for the settlement of the accounts relating to the Common Fund the opportunity to do so.

Let us briefly turn from theoretical considerations to the practical aspects of this subject. At the time of making the first investment of any estate, trust or fund in a Common Fund, notice thereof must be given to each person of full age and sound mind whose name and address is known to the Trust Company, who is then entitled to share in the income of the estate, trust or fund or who would be entitled to share in the principal in the event it were then distributable, and such notice must be accompanied by copies of those portions of the statute relating to the settlement of Common Fund accounts (McKinney's Consolidated Laws of New York, Banking Law §100-c, subdivision 9). In view of this there can be no reasonable doubt that any of the beneficiaries who desire to have the opportunity to examine such accounts and be heard upon the settlement thereof may, without inconvenience, arrange to learn when such accounts are presented for settlement.

Experience in connection with the settlement of other trustees' accountings show that most beneficiaries do not appear in such proceedings, that in many instances it is only the guardians appointed for minors or incompetents who assume the burden of examining such accounts and requiring the trustee to explain questionable conduct or restore the trusts if breaches of trust have occurred. In saying this, there is no wish to indicate that there are not a good many adult beneficiaries, who are represented by competent counsel who perform their full duties in connection with such proceedings, but the great majority do not. Under the New York statute, however, none of the beneficiaries will be unrepresented on the settlement of the accounts relating to a Common Fund. The court is required to appoint a competent attorney to represent all who do not

appear personally or by their own counsel, and, to be sure that those interested in the income are not favored at the expense of those who may share in the principal, or *vice versa*, a separate representative is appointed for each group. (McKinney's Consolidated Laws of New York, Banking Law, §100-c, subdivision 12).

While there is no great experience upon which to draw, it appears that the courts are aware of the importance of the duties cast upon these attorneys, and take pains to select those who are highly trained in these fields and fully qualified to deal with all questions arising in such proceedings.

The statutes of no other state have taken as much pains to afford full and adequate protection to the beneficiaries of trusts participating in Common Funds. (See Appendix C to appellant's brief, pp. 105-10).

It is submitted, therefore, that the questions presented on this appeal involve merely *technical legal theories.*

Since these have been fully briefed by the parties, the court shall not be burdened with any extended discussion but the matter shall be limited to a few brief observations.

II.

A proceeding for the settlement of an account of the trustee of a Common Fund is a proceeding *in rem.*

The appellant contends that such a proceeding is not solely one *in rem*, but in various aspects must be deemed to be a proceeding *in personam*. This is the basis of substantially the whole argument of the appellant. His contention that the notice required by the statute is not adequate rests upon this proposition (brief pp. 58-66).

This contention of the appellant would affect not only the Common Fund statute, but all proceedings for settle-

ment of accounts of trustees, executors, administrators and other fiduciaries. There are few such proceedings where personal service within the state may be effected on all parties having an interest in the estate, trust or fund to which the accounting relates. If the appellant is correct in his contention, then it would follow that the judgments and decrees settling the accounts of such trustees and other fiduciaries, which have been rendered by the courts of New York State and other states since their inception, are valid and effective only as to those persons upon whom personal service of the original process, in the actions or proceedings in which such judgments were rendered, was effected within the state in which such action or proceeding was instituted and, possibly in some jurisdictions, on persons who were residents of such state. It would follow also that no statute may be framed by the New York State Legislature which could cure the defect. Either these proceedings or actions for settlement of such accounts are *in rem*, or New York State courts may not render a judgment which will be binding on nonresidents unless they be served with process within the state.

Not only will our courts be unable effectively to settle the accounts of a trustee of a Common Fund, they will be unable effectively to settle the accounts of any fiduciary unless all parties having an interest therein are residents or within the State of New York; but experience shows that it is rare that all parties to such a proceeding or action are residents of or within the state.

In such a situation the wisdom of Judge Holmes is comforting. "Upon this point a page of history is worth a volume of logic." (*New York Trust Company* v. *Eisner*, 256 U. S. 345, 349.)

The appellant attempts to avoid the necessary result of his own argument by asserting that no claim is made that the requirements of due process in the present situ-

ation necessitate the personal service of a citation upon any and all interested persons (appellant's brief p. 13). Indeed, he seems to suggest that mailing of the notice of application to those currently interested in income would be acceptable (appellant's brief p. 37). The appellant's argument proves too much for if the proceeding be divisible, i.e., partly *in rem* and partly *in personam*, as he contends, then to effectuate the *in personam* aspects of the decree, personal service is required. In no other way would personal jurisdiction be obtained over non-residents. The fact is that, however, that the proceeding is not divisible; it is *in rem* and not *in personam*.

It is not necessary to rely merely on history, for theory and logic in this instance are in agreement with the history of such actions and proceedings.

In all such actions or proceedings the trust *res* is within the state and the courts of our state, therefore, have jurisdiction over the *res* and may adjudicate the rights and interests of all persons interested therein. The authorities cited by the appellee-trustee adequately support this proposition (brief of respondent-trustee, pp. 14-19).

The trust *res* usually consists not only of real and tangible personal property within the state, but for the most part, and in many instances exclusively, of intangible personal property represented by claims against various persons and corporations, some of whom may be within the state, but many of whom are without the state, plus shares or interests in corporate enterprises both within and without the state. *In addition, the trust res also includes any claim that may exist against the trustee for any breach of trust.*

Since this last mentioned asset of the trust, *i.e.*, the claim against the trustee for any breach of trust, is also part of the trust *res*, the courts of New York State have quite as much jurisdiction over this part of the *res* as they

have over any other asset of the trust. They may adjudicate the rights and interests of all persons interested in the estate, trust or fund in such assets, if any, which belong to the trust. That such right or claim is an asset of the trust is apparent, for the usual judgment of New York courts in such matters is that the trustee shall pay or transfer to the trust or stand charged with such moneys or property as the courts determine do or should form part of the trust.

Thus it is that a person who is not a resident of the state or is not personally served within the state may be judicially estopped from later asserting a claim of the trust estate against the trustee, for our courts upon the settlement of the accounts of a trustee determine the status of the trust and all the assets of the trust. They may determine as to all that the trust does not include among its assets a claim against the trustee.

Of course, a personal judgment may be rendered against the trustee, but when the trustee accounts, he submits himself to the jurisdiction of the court, and a judgment *in personam* may be rendered against him. However, the courts recognize their lack of jurisdiction to render a judgment *in personam* against anyone else over whom the court has not personal jurisdiction. If it is found that such an absentee has taken possession of an asset of the trust, the courts of New York state are incompetent to require the return of that asset. Either the trustee or the beneficiaries must sue in the state where such person may be found to effect such recovery.

The fact that judgments *in personam* may be rendered in such actions or proceedings against the trustee or others over whom the court acquires personal jurisdiction, in no way destroys the jurisdiction of the court over the trust *res* or detracts from the conclusion that an action or proceeding for the settlement of the account of a trustee, when the trust *res* is within the state, is an action or proceeding *in rem*.

III.

Since proceedings for the settlement of the accounts of a trustee of a Common Fund are *in rem*, the notices provided by the statute are adequate to conform to the constitutional requirements of due process of law.

It is respectfully submitted that the decisions of this court and of the New York State Court of Appeals abundantly demonstrate *first*, that in a proceeding *in rem* public advertisement in a newspaper for four weeks, clearly setting forth the nature of the proceeding and also identifying the names of all estates, trusts and funds having an interest in the Common Fund, is adequate to meet the constitutional requirements of due process of law, and *second*, that the courts will not endeavor to substitute their judgment for that of the Legislature as to the manner in which such notice should be given so long as the legislative determination is reasonable.

As to sufficiency of notice, see:

Goodrich v. *Ferris*, 214 U. S. 71.
Matter of Horton, 217 N. Y. 363;

As to the courts' not substituting their judgment for that of the Legislature, see:

Bellingham Bay Co. v. *New Whatcom*, 172 U. S. 314, 318;
Goodrich v. *Ferris* (*supra*, p. 81).

The decree and order appealed from should be affirmed.

Respectfully submitted,

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Of Counsel.